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C O N F I D E N T I A L SECTION 01 OF 02 KATHMANDU 000267

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SUBJECT: NEPAL-INDIA TRANSIT TREATY EXTENDED ONLY THREE MONTHS

Classified By: Ambassador James F. Moriarty, reasons 1.4 (b/d)

SUMMARY

11. (C) India and Nepal agreed at meetings held in New Delhi at the beginning of January to extend the Indo-Nepal transit treaty for three months instead of renewing it for seven years. The treaty provides for smooth movement of commercial goods through India, Nepal's largest trading partner. In 1989, after a similar interim extension period had expired, the Government of India (GOI) virtually shut down the Indo-Nepal border, crippling Nepal's economy. The head of the Nepali delegation believes that business issues unrelated to the treaty was the cause for India agreeing only to an interim agreement. End Summary.

TREATY EXTENDED ONLY THREE MONTHS

12. (SBU) India and Nepal could only agree to extend the Indo-Nepal transit treaty for three months rather than sign another seven year treaty at review meetings held January 4-5 in New Delhi. The treaty provides conditions for the movement of commercial goods between India and Nepal. As 61 percent of Nepal's total trade is with India, Nepal's economy depends largely on the ability to move goods freely and efficiently through its border with India and Calcutta port. There has been an Indo-Nepal trade treaty since 1950, with the issue of transit points first appearing in a 1971 treaty renewal. In 1989, after a similar treaty extension period had passed, India closed the majority of transit points with Nepal over political differences and crippled Nepal's economy. The current transit treaty went into effect on January 6, 1999, and called for a seven year extension after it expired on January 5, 2006, pending review by both countries. India had notified His Majesty's Government of Nepal (HMGN) that it wished to review the treaty in November 12005. HMGN and GOI officials have not yet made plans for further review meetings.

UNABLE TO REACH AGREEMENT ON KEY POINTS

13. (C) The GOI named five points of concern for review in the meetings: the rationalization of transit points; a guarantee system to protect third-country shipments; the movement of sensitive goods to prevent smuggling; the

incorporation of the existing rail services agreement into the transit treaty; and the ability to ship goods from one point in India to another, via Nepal. Jawed Ashraf, Economic Officer at the Indian Embassy in Kathmandu, lamented to Emboff that "Nepal expected India to just renew the treaty and accept what Nepal wanted without giving any responses to our inquiries." Naindra Upadhayay, Joint Secretary at the Ministry of Industry, Commerce and Supplies and head of the Nepal delegation, told Emboff that Nepal had been prepared to agree to all of the GOI delegation's terms, but the Indian delegation had claimed it needed approval from higher authorities to finalize the treaty. Ashraf said the lack of responses from Nepal had resulted in the necessity for a three month interim extension of the treaty.

Rationalization of Transit Points

14. (C) Most important to Nepal are the 15 transit points on the Indo-Nepal border provided for in the treaty. Upadhayay asserted India had proposed to reduce the number of transit points, to which he had argued that more transit points would benefit both countries in light of Nepal's World Trade Organization (WTO) commitments and the changing global trade regime. Ashraf stressed that the GOI "desired to be extremely accommodating" on transit points; rationalization did not necessarily mean reducing the number of transit points, but Nepal should justify the need for the 15 points.

Bank Guarantee for Third Country Shipments

15. (C) HMGN worried that the Indian proposal that all third-country shipments transiting India have a bank

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guarantee to guard against liability issues for stolen shipments would be costly for Nepal. Upadhayay explained that a bank guarantee requirement would raise the already high transportation costs for Nepali shippers, increasing the cost of Nepali imports and exports.

ISSUES RAISED BY INDIA ON SIDELINES - AGREEMENT STOPPERS?

16. (C) Upadhayay explained that on the sidelines of the transit treaty review meetings, the Indians had raised an on-going dispute regarding United Telecom Limited (UTL), and expressed a desire for a change in Nepal's current foreign employment laws for Indians. He opined that these issues were the main cause for India deferring renewal of the transit treaty. He also mentioned that other "political concerns" might have played a part in India's decision. The Joint Secretary worried that the GOI delegation had decided in advance of the review meetings only to extend the transit treaty for three months. He noted that the Indian Ministry of Commerce had faxed an extension letter for the Nepal Commerce Secretary's signature while the review meeting was still on-going in New Delhi.

United Telecom Losing Money in Nepal

17. (SBU) UTL, an Indo-Nepal telecom joint venture, owned 80 percent by Indian government agencies and 20 percent by a private Nepali company, has a history of complaints about doing business in Nepal. Three years ago, the Supreme Court prevented UTL from importing smaller Code Division Multiple Access (CDMA) cell phones to Nepal. UTL claimed its inability to introduce smaller CDMA handsets greatly reduced the company's competitiveness in Nepal's mobile phone market. Other grievances include the loss of revenue caused by the disruption of UTL wireless phone service after the February 1 royal takeover. UTL believes HMGN discriminated against them in favor of Nepal Telecom, which recently has been given approval to use CDMA technology. UTL wireless service was

down from January 19 to January 26 when HMGN cut wireless service before scheduled mass demonstrations, causing UTL a loss of approximately USD 280,000 a day, whereas the government allowed Nepal Telecom to restore service to post-paid cell phones on January 23.

India Wants Foreign Employment Rules Changed for Indians

18. (SBU) A 1950 Treaty for Special Treatment to Nepalese allows Nepalese to work in government or private sector jobs in India and own property without limit. India has been pressing Nepal to reciprocate and allow Indian citizens to work in Nepal without limit. Current Nepali law limits expatriates to a maximum three year period to work in Nepal; however, Indians are not required to obtain visas to work in Nepal.

COMMENT

19. (C) It is unclear whether the three month extension is really tied to the UTL or foreign employment law issues or a GOI reminder to Nepal of its dominant position and ability to hold Nepal's economy hostage as it did in 1989. India has once again shown it could use the transit treaty negotiation points as political leverage and continue to stall treaty renewal, vital for Nepal.

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